

Local governments provide an array of other benefits to their retirees including things like health care, vision, dental and other benefits, collectively referred to as Other Post Employment Benefits (OPEB). The largest component of OPEB is retiree health care. According to the Government Finance Officers Association (GFOA) 1998 publication Prefunding Retiree Health Benefits, 74 percent of state governments and 57 percent of local governments provide health benefits to retirees over age 65. Approximately the same percent provide health benefits to retirees under age 65. In 2002, a study by the Municipal Employees' Retirement System of Michigan showed that 74 percent of the 353 municipal respondents provided retiree health care, with most offering both pre-65 and post-65 coverage.

Most of these arrangements resulted from negotiations with bargaining units at a time when employers could sponsor retiree health care for a few tenths of a percent of active employee payroll. More recently approved labor contracts have built on the labor contracts reached in the older, more established communities. The rapid increase in health care costs has increased the impact of this benefit on local budgets significantly. Most governmental employers have been financing the benefits on a pay-as-you go basis.

In June 2004, the Government Accounting Standards Board (GASB – the organization that prescribes accounting standards for governmental entities), approved the final set of accounting standards applicable to OPEB, known as GASB 45. The GASB's standards apply differently depending on whether the benefit is provided through a defined benefit plan or a defined contribution plan. For benefits provided through defined benefit plans, the primary requirement is that the long-term cost of the benefit (e.g. retiree health care) be measured and reported on the accrual basis using actuarial methods and assumptions applied in essentially the same way that they are applied to pension plans. Translated – this means that units of local government will have to fund these future costs on a present basis or their finances will show a deficit.

Translated another way, what this means is that governmental units such as the City of Grand Rapids will be required to conduct actuarial valuation studies on an annual basis. These actuarial reports will show that the unfunded liability for post retirement benefits such as retiree health care exceed 1.1 trillion dollars nationwide. Approximately 30 percent of the states have unfunded liabilities in excess of 5 billion dollars. The City of Grand Rapids has unfunded liability in excess of 155 million dollars. Actuaries report that the Retiree Health obligation (both past and future commitments to provide benefits) now costs 14% to 28% of current payroll.

The City finds itself in this situation because it has chosen to fund the liability to fund the promised benefits at the time the individual retires rather than funding the cost over the period of the individual's employment. To further illustrate my point, the City's obligation for retiree health benefits that have been earned in prior years for Police Officers exceeds \$165,000 for every active Police Officer. Recognizing that the liability will only continue to grow, the City Commission took the bold steps to begin partial amortization of these liabilities two years ago.

The fact of the matter is that even partially funding the actuarial required contribution has become a point of contention in budget deliberations and collective bargaining with the unions asserting that our recommended funding is addressing the problem too quickly. My response has been that we aren't even fully funding the actuarial contribution and even if we were, it would still take 30 years to pay off this debt. Now there is no magical solution to resolve this problem in a manner that will be acceptable to all parties. For example, current taxpayers have difficulty understanding why they should be asked to pay for costs that are not related to the current services being provided. Employees and retirees ask and expect that the benefits that they anticipated throughout their

working career will be provided. At the end of the day, compromise will be required from all parties.

One tool that should be made available on an explicit permissible basis is the ability of local governmental units to fund a portion of this past liability with bonded debt. The proceeds of which would be invested in a manner similar to pension assets. Make no doubt about it that this tool will not in of itself solve the problem, but it is another arrow in the quiver. The City of Grand Rapids has estimated that if we were to bond this liability and take proceeds and invest them like we do pension assets that the savings would be nearly 18 percent or 21 million dollars. This analysis assumes that we would only fund 75 percent of the accrued liability. The reason we have settled on the 75 percent number is because we recognize that there is a risk associated with investing such a large amount of dollars into the market assets at a single point in time. If the market goes down, the problem has become worse, at least initially. Perhaps a greater fear, believe it or not, is what if the market goes up dramatically. Experience tells me that when assets contained in an irrevocable trust fund exceed the amount of the liability, that pressure will build to improve the benefits those assets are intended to pay for. Improvement of those benefits will obviously result in increased costs.

So in conclusion, I would request that this bill that would permit bonding for post employment benefits be given fair consideration, but I would also ask that the Legislature retain the safeguards that were in the proposed legislation.

Those safeguards should include, at a minimum, the requirement that a governmental unit shall have first prepared actuarial studies. A plan can not be developed until the problem is thoroughly understood. Second, that the governmental unit shall be prepared to develop a plan for how it intends to manage liability. My concern is that unsophisticated governmental units could be

led to believe that they can bond their way out of this problem. As I have said earlier, I do not believe this is possible. Thank you for your consideration today.